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IN THE

Supreme Court of the United States

October Term, 1982

CONTAINER CORPORATION OF AMERICA,
Appellant,
v.
FRANCHISE TAX BOARD,
Appellee.

On Appeal from the Court of Appeal of the State of California for the First Appellate District

BRIEF OF THE STATE OF NEW MEXICO AS AMICUS CURIAE IN SUPPORT OF THE FRANCHISE TAX BOARD

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QUESTIONS PRESENTED

1. Whether standards exist for the determination whether foreign commerce is an issue in this case.

2. Whether foreign commerce is necessarily burdened by the imposition of a fairly apportioned tax on the income of a multinational unitary business.

3. Whether multiple burdens of taxation alone are proscribed by the commerce clause.

4. Whether a broad national policy pre-emption standard is warranted in determining the validity of a state income tax and whether, under such a broad standard, California's franchise tax is invalid.

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BRIEF OF THE STATE OF NEW MEXICO AS AMICUS CURIAE IN SUPPORT OF THE FRANCHISE TAX BOARD

INTEREST OF THE STATE OF NEW MEXICO

Container Corporation of America challenges California's franchise tax, imposed under an apportionment formula which is applied to Container's worldwide operations, on due process and commerce clause grounds. Container argues that California's tax misapportions income to domestic members of its

operations, thus overreaching, in violation of the due process clause. Additionally, Container argues that California's tax results in multiple burdens of taxation, and that California's use of the apportionment method on its worldwide income conflicts with the federal system of arms-length reporting, thus preventing the federal government from speaking with one voice in matters of foreign commerce. On these grounds Container argues that the tax violates the commerce clause. Container also argues that it does not conduct a unitary business with its foreign subsidiaries.

New Mexico employs the unitary apportionment method of determining the income of multijurisdictional corporations. It is vitally interested in the Court's resolution of the issues presented in this case. This brief is therefore submitted in support of the Franchise Tax Board and the validity of California's tax.

SUMMARY OF ARGUMENT

Container seeks to show that it does not conduct a unitary business with its foreign subsidiaries. Although Container raises this point at the end of its brief, the unitary question must be addressed before California's tax may be analyzed under the due process and commerce clauses. This brief assumes a unitary operation and a tax valid on due process grounds as a basis for its discussion of the commerce clause issues raised by Container.

Container argues that California's franchise tax, imposed on its worldwide operations, violates the commerce clause because it burdens foreign commerce. However, Container has not shown that foreign commerce is an issue in this case. Applying *Bass, Ratcliff & Gretton, Ltd. v. State Tax Commission*, 266 U.S. 271 (1924) and the accepted bases of the apportionment method of determining income to the facts of this case, the Court must find that foreign commerce is not burdened by the

imposition of a fairly apportioned tax on a multinational unitary business.

Container asks the Court to invalidate California's tax under the two-part foreign commerce test established in *Japan Line, Ltd. v. County of Los Angeles*, 441 U.S. 434 (1979). *Japan Line* is not applicable to this case because, under the holding of *Bass, Ratcliff*, foreign commerce is not an issue. However, even should the Court find that foreign commerce is an issue here, *Japan Line* should not be followed. *Japan Line* imposed a proscription against multiple burdens of taxation when foreign commerce is involved. However, multiple burdens of taxation alone are not proscribed by the commerce clause. *Japan Line* held that a state tax will be held invalid when it interferes with the achievement of federal uniformity in the field of foreign relations. The Court thus pre-empted a state tax on the basis of general national policy. The national policy standard has been rejected in pre-emption analysis. Additionally, even under a broad pre-emption standard, Container cannot prevail in its argument, because it has not shown the existence of a national policy which governs state taxation of the income of multijurisdictional corporations.

ARGUMENT

I

NO STANDARDS EXIST FOR THE DETERMINATION WHETHER FOREIGN COMMERCE IS AN ISSUE IN THIS CASE.

Container argues that imposition of California's franchise tax on an apportioned part of the combined income realized from its worldwide operations burdens foreign commerce and violates the commerce clause of the Constitution. (Brief of Appellant at 21) Container urges the Court to apply *Japan Line,*

Ltd. v. County of Los Angeles, 441 U.S. 434 (1979) and invalidate California's tax under the two-part test announced in that case.[1]

It is necessary to the invocation of *Japan Line* that foreign commerce be an issue in this case. Container contends that it is. The basis of Container's contention is unclear, however. Container's foreign commerce argument contains two threads: 1) that California's apportionment formula overreaches, misattributes income and thus taxes foreign profits (Brief of Appellant at 11, 21); and 2) that because multinational corporations may be subject to multiple tax burdens and because there is a need for federal uniformity in the area of foreign commerce, the taxation of multinational corporations necessarily implies a foreign commerce question. (Brief of Appellant at 21-39) Container has tangled the threads of its argument and invites the Court to invalidate combined reporting as applied to multinational businesses on foreign commerce grounds alone. (Brief of Appellant at 37)

Logically, however, Container's argument must be analyzed in two stages. First, it must be determined whether California's apportionment formula, as applied to Container's worldwide business, overreaches. If the Court finds that it does, the tax is invalid under the due process clause and there is no need to reach the foreign commerce question. If it does not, the Court must then address the question whether taxation of a multinational corporation under an acceptable apportionment formula necessarily involves foreign commerce. Crucial to the second determination is a knowledge of what constitutes foreign commerce for tax purposes. Although Container and its *amici* make facile use of the term "foreign commerce," there is no indication that the term has a commonly accepted meaning.

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1 The elements of the test are 1) whether the tax subjects foreign commerce to multiple tax burdens, and 2) whether the tax impairs federal uniformity. *Japan Line*, 441 U.S. at 448.

When analyzing state taxes which are alleged to burden interstate commerce, there is no longer a need to quibble over what does or does not amount to interstate commerce for tax purposes.[2] In this Court's decision in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 288-89 (1977), the rule, enunciated in *Spector Motor Service v. O'Connor*, 340 U.S. 602 (1951), that certain aspects of interstate commerce were immune from taxation was flatly rejected. The Court then adopted the far more workable rule that a state could tax activities in interstate commerce as long as its tax met certain criteria. Because *Japan Line* imposed a separate commerce clause test for analyzing taxes which are alleged to burden foreign commerce, the Court immunized foreign commerce from state taxation in certain circumstances. Thus, in the area of foreign commerce, *Japan Line* has brought us back to the same abstract and difficult questions previously presented in interstate commerce analysis. Tax administrators, taxpayers and eventually the courts must once again struggle to define foreign commerce and to devise tests to separate purely foreign commerce from the complicated system of local, interstate and foreign commerce in which modern business operates.[3]

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2 *See Commonwealth Edison Co. v. State of Montana*, 453 U.S. 609, 614-15 (1981) and n. 3, *infra*.

3 Since it was thought that the commerce clause prohibited states from directly taxing interstate commerce, it became necessary to distinguish local from interstate commerce. *See, e.g., Dunbar-Stanley Studios, Inc. v. Alabama*, 393 U.S. 537 (1969) (photography is local event, and so taxable, although photographer is out-of-state corporation); *Alaska v. Arctic Maid*, 366 U.S. 199 (1961) (tax on freezer ships is tax on local activity, even though fish are transported out-of-state after freezing); *Norton Co. v. Department of Revenue*, 340 U.S. 534 (1951) (when sale can be attributed to local business activities, gross receipts of out-of-state company are taxable); *Western Live Stock v. Bureau of Revenue*, 303 U.S. 250 (1938) (tax on sale of advertising space in magazine with interstate circulation is

(Cont. p. 6)

However, the *Japan Line* decision does not provide a definition of foreign commerce which may be applied to the facts of this case. Because of the unique characteristics of the containers taxed in *Japan Line*, the Court addressed the question of whether foreign commerce was involved in one sentence: "Appellants' containers, however, are instrumentalities of foreign commerce, both as a matter of fact and as a matter of law." 441 U.S. at 445-46 (footnotes omitted). Perhaps it is easier to identify "instrumentalities of foreign commerce," *id.*, than to determine generally what foreign commerce may be for tax purposes. It is clear, however, that the issue of whether taxation of multinational business presents the kind of foreign commerce question the Court addressed in *Japan Line* is a complex one, and one which has not been adequately addressed by Container.

Subsequent to its decision in *Japan Line* that foreign commerce is to be treated differently from interstate commerce, *id.* at 446, the Court has not provided guidance on when that treatment will be afforded. In *Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. 425 (1980), the Court declined to apply *Japan Line* to a case involving income taxes, stating that "the

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3. (Cont. from p. 5)
permissible because preparing and printing advertising is local event); *Oliver Iron Mining Co. v. Lord*, 262 U.S. 172 (1923) (mining is a local activity, and so taxable despite fact that ore will be shipped out-of-state). The distinction between local and interstate activities, difficult and sometimes arbitrary, leads to anomalous results. *Compare, e.g., East Ohio Gas Co. v. Tax Commission*, 283 U.S. 465 (1931) (transmission of gas to Ohio municipalities under low pressure is local business and so taxable) with *State Tax Commission v. Interstate Natural Gas Co.*, 284 U.S. 41 (1931) (transmission of gas to distributors in Mississippi part of interstate commerce and so not taxable). This approach was finally found unworkable in the area of interstate commerce. *Commonwealth Edison Co. v. Montana*, 453 U.S. 609 (1981). It may prove to be equally unworkable in the area of foreign commerce.

factors favoring use of the allocation method in property taxation have no immediate applicability to an income tax." *Id.* at 448. Thus, although the Court in *Mobil* did not offer guidance on what foreign commerce is for state taxation purposes, its opinion indicates that foreign commerce is not burdened by the application of a fairly apportioned tax on unitary income.[4]

II

THE IMPOSITION OF A FAIRLY APPORTIONED TAX ON THE INCOME OF A MULTINATIONAL UNITARY BUSINESS DOES NOT BURDEN FOREIGN COMMERCE.

Although it is unclear what foreign commerce is for tax purposes, the holding of *Bass, Ratcliff & Gretton, Ltd. v.State Tax Commission,* 266 U.S. 271 (1924)[5] indicates that this case does not present a foreign commerce issue. In that case, a foreign corporation contended that the application of New York's franchise tax to an apportioned share of the profits realized by the corporation in conducting its unitary business imposed a burden on foreign commerce and thus violated the commerce clause. The Court found that where a corporation conducts a unitary business both within and without the country, New York could tax a proportionate share of the profits earned by

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4 The *Mobil* Court cited *Bass, Ratcliff & Gretton, Ltd. v. State Tax Comm'n,* 266 U.S. 271 (1924). 445 U.S. at 438.

5 Container seeks to characterize *Bass, Ratcliff* as so outmoded as to be inapplicable. (Brief of Appellant at 8, n. 2) However, this Court in *Mobil,* 445 U.S. at 438, apparently found it was still viable, citing it as the "leading example" of the application of the rationale that "factors of profitability arise from the operation of [a] business as a whole, [thus] it becomes misleading to characterize the income of the business as having a single identifiable 'source,' " 445 U.S. at 438, to "businesses operating both here and abroad." *Id.*

the corporation without offending the commerce clause, as long as the tax was "based upon the portion of such ascertained net income determined by the proportion which the aggregate value of specified classes of the assets of the corporation within the State bears to the aggregate value of all such classes wherever located." *Id.* at 278. The Court's conclusion that New York's tax did not burden foreign commerce was based on the accepted principle that a proper method of apportionment, applied to the combined income of a unitary business, " 'reache[s], and [is] meant to reach, only the profits earned within the [taxing] State.' "[6] *Id.* at 281 (quoting *Underwood Typewriter Co. v. Chamberlain*, 254 U.S. 113, 121 (1920)).

Bass, Ratcliff is directly applicable to this case. Container's attempts to distinguish it (Brief of Appellant at 8, n. 2) are not persuasive. Container first argues that *Bass, Ratcliff* is not controlling because the corporation in that case did not operate through subsidiaries, but rather through operating divisions. This argument ignores the teaching of *Mobil* that the "form of business organization may have nothing to do with the underlying unity or diversity of business enterprise." 445 U.S. at 440. Second, Container argues that the taxpayer in *Bass, Ratcliff* did not allege that New York's apportionment formula misattributed income and hence the case is inapposite. This

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6 In the hysteria produced by the sanctity of foreign profits the fact that a proper apportionment formula will not reach them is overlooked. Yet this Court has stated that a proper formula will "reflect 'the relative contribution of the activities in the various states to the production of the total unitary income,' so as to allocate to [the taxing state] its just proportion of the profits earned by appellant from this unitary business." *Butler Bros. v. McColgan*, 315 U.S. 501, 509 (1942). The underlying premise of the apportionment process is that it allows the taxing state to tax only those profits which are attributable to it. *Central Greyhound Lines, Inc. v. Mealey*, 334 U.S. 653 (1948).

argument reflects the confusing approach Container takes in this case.[7] Container's allegation of misattribution of income is pertinent to this Court's determination of first, whether Container is a unitary business and second, whether California's apportionment formula adequately determines Container's California income. If the Court answers these two questions in the affirmative, *Bass, Ratcliff* is directly applicable to the next issue before the Court: whether application of an acceptable apportionment formula to a multinational unitary business burdens foreign commerce. *Bass, Ratcliff's* unequivocal answer is that it does not. Therefore, should the Court find that California's apportionment formula meets due process standards, the Court should find that *Bass, Ratcliff* is controlling and foreign commerce is not burdened in this case. To apply *Japan Line* and its foreign commerce test would necessitate overruling *Bass, Ratcliff* and the cases which follow it.

III

SHOULD THE COURT FIND THAT THIS CASE PRESENTS A FOREIGN COMMERCE QUESTION, *JAPAN LINE* SHOULD NOT BE FOLLOWED.

In *Japan Line* the Court held that where foreign commerce was at issue, a challenged tax must meet two tests in addition to those imposed by *Complete Auto Transit.* These tests are 1) whether the tax subjects foreign commerce to multiple tax burdens, and 2) whether the tax prevents the federal government from speaking with one voice in its relations with foreign nations. The multiple burdens test is not compelled by the Constitution. The broad pre-emption standard developed under the federal uniformity test is not warranted under the supremacy clause. Container does not show that California's tax is pre-empted even under the broad standard imposed. For these reasons the *Japan Line* tests should not be applied in this case.

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[7] *See* Part I, *supra.*

A. Multiple Burdens Alone Are Not Proscribed By The Commerce Clause.

The first part of the extended foreign commerce test established in *Japan Line* is that the questioned tax must not subject foreign commerce to multiple burdens of taxation. The Court in *Japan Line* introduced its multiple burden test with the statement that "[i]t is a commonplace of constitutional jurisprudence that multiple taxation may well be offensive to the Commerce Clause." 441 U.S. at 446. The Court cited the "enhanced risk" of multiple burdens in the area of foreign commerce as the basis for imposition of this test.[8] *Id.* However, multiple burdens of taxation without more are not proscribed by the commerce clause.[9] While the term "multiple burdens" is often used to call into question the constitutionality of state taxing schemes, the doctrine underlying the term is complex

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8 One commentator suggests that the Court's decision to develop a different standard for foreign commerce questions was based on an attempt to apply a doctrine of interstate commerce which prohibits *states* from imposing undue burdens on commerce, to international commerce, an application which cannot logically be made. The Court in *Japan Line* reasoned that because Japan taxed the containers in full, California's tax was prohibited. However, the commentator argues, the only commerce clause inquiry the Court in *Japan Line* need have made was whether California's tax burdened commerce. Japan's imposition of a tax was irrelevant to this inquiry as was the Court's inability to require that Japan's tax be apportioned. Note, *Constitutional Law – The Scope of the Commerce Clause in International Commerce*, 55 WASH.L.REV. 885, 892 (1979); *see Mobil:* "[I]t [Mobil's argument] attempts to focus attention on the effect of foreign taxation when the effect of domestic taxation is the only real issue." 445 U.S. at 447. If the Court's inquiry under the commerce clause is limited to whether a state tax has unduly burdened commerce, a separate foreign commerce test is unnecessary.

9 None of the cases cited by the Court in support of its statement that multiple taxation may offend the commerce clause held that multiple burdens alone are forbidden. Rather multiple burdens which resulted in

(Cont. p. 11)

and embodies two important aspects of commerce clause analysis, *i.e.*, that taxes which impose discriminatory multiple burdens on interstate commerce are forbidden, and that taxes imposed upon interstate commerce must be fairly apportioned.

The origins of the multiple burden test in commerce clause analysis may be found in *Western Live Stock v. Bureau of Revenue*, 303 U.S. 250 (1938). That case announced that multiple taxation, while not in itself unconstitutional, could violate the commerce clause if it resulted in a cumulative tax burden which discriminated against interstate commerce. Other cases have also indicated that multiple taxation is repugnant to the commerce clause only when it causes interstate commerce to bear a greater tax burden than local commerce. *See Evco v. Jones*, 409 U.S. 91, 94 (1972); *Standard Oil Co. v. Peck*, 342 U.S. 382, 384-85 (1952); *Ott v. Mississippi Valley Barge Line Co.*, 336

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9. (Cont. from p. 10)
discrimination against interstate commerce were found invalid under the clause, as were taxes which were not fairly apportioned. *Evco v. Jones*, 409 U.S. 91, 94 (1972) (tax invalidated because it subjected interstate commerce to risks of a double tax burden to which intrastate commerce was not exposed); *Central R.R. Co. v. Pennsylvania*, 370 U.S. 607, 614 (1962) (tax by domiciliary state of *full value* of rolling stock invalid where other states could apply apportioned taxes); *Standard Oil Co. v. Peck*, 342 U.S. 382, 384-85 (1952) (tax invalidated because it imposed multiple burdens on vessels engaged only in interstate commerce); *Ott v. Mississippi Valley Barge Line Co.*, 336 U.S. 169, 174 (1949) (tax valid because "[it] has no cumulative effect caused by the interstate character of the business . . . [and] seems therefore to square with our decisions holding that interstate commerce can be made to pay its way by bearing a nondiscriminatory share of the tax burden which each State may impose on the activities or property within its borders."); *J. D. Adams Manufacturing Co. v. Storen*, 304 U.S. 307, 311 (1938) (tax invalid because it would subject interstate commerce "to the risk of a double tax burden to which intrastate commerce is not exposed.") None of these cases invalidated an apportioned tax imposed by a jurisdiction with an appropriate claim to tax.

U.S. 169, 174 (1949); *J. D. Adams Manufacturing Co. v. Storen*, 304 U.S. 307, 311 (1938). This Court has stated that the fundamental principle to be applied in commerce clause analysis is: "No State, consistent with the Commerce Clause, may 'impose a tax which discriminates against interstate commerce. . . .' [citations omitted]. The prohibition against discriminatory treatment of interstate commerce follows inexorably from the basic purpose of the Clause." *Boston Stock Exchange v. State Tax Commission*, 429 U.S. 318, 329 (1977) (quoting *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 458 (1959)).

The broadening of the states' power to tax interstate commerce, announced in *Western Live Stock* and the cases which followed it, was accompanied by the requirement that a tax imposed by a state be apportioned by methods which reflected the state's connection with the object of taxation.[10] Because the commerce clause prohibits multiple burdens of taxation which fall only on interstate commerce, and because more than one jurisdiction may have the right to tax interstate commerce, apportionment became essential to validation of a state tax under the commerce clause.[11] Where a tax is fairly apportioned there can be no multiple tax burden. *Japan Line*, 441 U.S. at 447-48; *see Mobil; Exxon Corp. v. Wisconsin Department of Revenue*, 447 U.S. 207 (1980); *Standard Pressed Steel Co. v. Washington Department of Revenue*, 419 U.S. 560 (1975). In the absence of a showing that a challenged tax is not properly apportioned, a multiple burdens claim may not successfully be made. *See Moorman Manufacturing Co. v. Bair*, 437 U.S. 267 (1978).

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10 The multiple burdens doctrine is linked with jurisdictional analysis under the commerce clause. *See* LAURENCE H. TRIBE, AMERICAN CONSTITUTIONAL LAW §6-17, at 361 (1978).

11 *See* JEROME R. HELLERSTEIN AND WALTER HELLERSTEIN, STATE AND LOCAL TAXATION 243 (4th ed. 1978).

The pertinent question in multiple burden cases is not whether one or more jurisdictions are taxing the same income, property or activity but rather whether the state in question is exacting a fair demand for the aspect of interstate commerce to which it bears a relation. *See Department of Revenue v. Washington Stevedoring Cos.*, 435 U.S. 734 (1978); *Central Greyhound Lines, Inc. v. Mealey*, 334 U.S. 653 (1948). The fact that two jurisdictions are imposing a tax on the same property or activity is not a sufficient basis for invalidation of a tax on commerce clause grounds.[12] If California's tax is found to be fairly apportioned and treats domestic, interstate and foreign commerce with an even hand, the imposition of a tax by other jurisdictions is not relevant to the validity of California's tax under the commerce clause.

Container's multiple burden theory is flawed in two significant respects. First, had California imposed a gross receipts tax instead of an income tax on Container's California operations the economic effect on Container would have been the same, yet Container would have no basis for complaint under its multiple burdens theory. *See Moorman*, 437 U.S. at 280. Under this theory it is the imposition of an "income" tax by more than one jurisdiction which invalidates the tax. It would be an exercise in formalism to find a tax invalid on the basis

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12 The Court in *Moorman* addressed the question whether Iowa's corporate income tax should be held invalid because, together with Illinois' tax, it allegedly subjected interstate commerce to multiple tax burdens. The Court stated that:

> [W]hatever disparity [in treatment of local and foreign corporations] may have existed is not attributable to the Iowa statute. It treats both local and foreign concerns with an even hand; the alleged disparity can only be the consequence of the combined effect of the Iowa *and* Illinois statutes, and Iowa is not responsible for the latter.

437 U.S. at 277, n. 12.

of speculative concerns with multiple taxation if the same tax, but with a different name, would be valid under the commerce clause.[13] *Id.*

Second, multiple taxation on the total value of property or on income is constitutionally valid when the taxes are imposed by jurisdictions with concurrent rights to tax. Concurrent federal and state taxation of income is a well-established norm. *Mobil*, 445 U.S. at 448. Death taxes on the same estate can be imposed by both the state and federal governments. *Frick v. Pennsylvania*, 268 U.S. 473 (1925). The Constitution does not prohibit taxation of real estate by two concurrent jurisdictions. *See Davidson v. New Orleans*, 96 U.S. 97 (1878). The allowance of multiple taxation by jurisdictions with concurrent rights to tax is based on the fact, long recognized by this Court, that the power to tax is a fundamental attribute of sovereignty. *Gibbons v. Ogden*, 22 U.S. (9 Wheat.) 1, 198-99 (1824). In this case California and the federal government have concurrent rights to tax Container's income. Presumably, California also enjoys such a concurrent right with foreign jurisdictions with rights to tax parallel to those of federal government. Yet Container argues that because another jurisdiction also imposes a tax on its income, California's tax must be held invalid. Container's argument is not persuasive in light of the case law cited above.

It is only when a challenged tax discriminates against commerce or is not fairly apportioned that a valid multiple burden claim may be made under the commerce clause. The *Complete*

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[13] It would be an equally formalistic approach to find California's tax invalid merely because another jurisdiction is also imposing an income tax where no facts about the nature or level of that tax are alleged or proved. Yet, in *Japan Line* the fact that Japan imposed a "property" tax was sufficient to call into question the validity of the county's tax. Facts about the actual nature, the level or the incidence of that tax were not required. 441 U.S. at 452, n. 17.

Auto Transit test incorporates these two requirements. 430 U.S. at 277-78. The Court in *Japan Line* held that the county's tax met these two tests, finding that the tax was not discriminatory and was fairly apportioned. 441 U.S. at 445. An additional proscription against multiple burdens alone in the area of foreign commerce is not compelled by the commerce clause. The imposition of the *Japan Line* multiple burdens test will preclude state taxation whenever a foreign jurisdiction imposes, or has the right to impose, a tax.[14] This result contravenes principles of federalism and ignores the states' sovereign right to tax. For these reasons the test should not be imposed in this case.

B. *Japan Line's* National Policy Pre-emption Standard Is Overly Broad; Even Under That Standard, However, California's Tax Is Not Pre-empted.

The second part of the foreign commerce test announced in *Japan Line* requires that a state tax be held invalid under the commerce clause if it prevents the federal government from speaking with one voice in matters of foreign commerce. The *Japan Line* Court cited the principle it established in *Michelin Tire Corp. v. Wages*, 423 U.S. 276, 285 (1976): " '[T]he Federal Government must speak with one voice when regulating commercial relations with foreign governments,' " 441 U.S. at 449, noting that "[t]he policies animating the Import-Export

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[14] The Court in *Japan Line* adopted an allocation approach and suggested that the mere possibility of multiple taxation will preclude a state tax. 441 U.S. at 446. In effect this approach is remarkably similar to that reached under the home port doctrine under which only the home port was allowed to tax a vessel engaged in interstate commerce. But the Court in *Japan Line* noted that the home port doctrine "has yielded to a rule of fair apportionment," 441 U.S. at 442, and "can claim no unequivocal constitutional source." *Id.* at 443.

Clause [under which *Michelin* was decided] and the Commerce Clause are much the same."[15] *Id.* at 449, n. 14.

Although not so demonimated, the one-voice test is essentially a pre-emption test. Under traditional pre-emption analysis "[p]re-emption of state law by federal statute or regulation is not favored 'in the absence of persuasive reasons – either that the nature of the regulated subject matter permits no other conclusion, or that Congress has unmistakenly so ordained.' " *Commonwealth Edison Co. v. Montana,* 453 U.S. 609, 634 (1981) (quoting *Chicago & North Western Transportation Co. v. Kalo Brick & Tile Co.,* 450 U.S. 311, 317 (1981)). Whether

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15 Although the Court cited *Michelin* with approval it did so without adopting the rationale or holding in that case. In *Michelin* an ad valorem tax was imposed on imported tires stored in a warehouse. Michelin claimed that imposition of the tax violated the import-export clause. The Court in *Michelin* found no violation of the clause, emphasizing the nondiscriminatory nature of the tax. The Court stated:

> It is obvious that such nondiscriminatory property taxation can have no impact whatsoever on the Federal Government's exclusive regulation of foreign commerce, probably the most important purpose of the Clause's prohibition. By definition, such a tax does not fall on imports as such because of their place of origin. It cannot be used to create special protective tariffs or particular preferences for certain domestic goods, and it cannot be applied selectively to encourage or discourage any importation in a manner inconsistent with federal regulation.

423 U.S. at 286. The reasoning applied under the import-export clause in *Michelin* may be applied to commerce clause questions as well. 441 U.S. at 449, n. 14. The *Japan Line* tax met the requirements of *Michelin:* it was "nondiscriminatory"; it did not fall on instrumentalities of foreign commerce because of "their place of origin"; it could not be used to protect domestic instrumentalities; and it could not "be applied selectively to encourage or discourage" commerce. 423 U.S. at 286. Yet, while the Court found the *Michelin* tax valid, it invalidated the county's tax in *Japan Line.*

a state law has been pre-empted by federal laws or treaties touching the same subject depends upon whether the state law "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941). A state law may be found to have been pre-empted either because of an actual conflict between the state and federal statutes or regulations, or by evidence of a congressional design to pre-empt the field. *Florida Lime & Avocado Growers, Inc. v. Paul*, 373 U.S. 132 (1963). Deciding whether a state statute is invalid under the supremacy clause because it conflicts with federal law " 'is essentially a two-step process of first ascertaining the construction of the two statutes and then determining the constitutional question whether they are in conflict.' " *Chicago & North Western Transportation Co. v. Kalo Brick & Tile Co.*, 450 U.S. at 317 (quoting *Perez v. Campbell*, 402 U.S. 637, 644 (1971)). This conflict can be found either in provisions contradictory on their face or from a conflict between the state statute and the objectives underlying the federal enactment. *See Jones v. Rath Packing Co.*, 430 U.S. 519 (1977). When no actual conflict exists, state law must yield only when the nature of the subject matter or an explicit declaration of congressional design to displace state law so requires, and federal occupation of a field will not be lightly inferred. *See Florida Lime & Avocado Growers.* Absent federal legislation a state may impose a system of taxation as long as that system is "within the restraints imposed by the Commerce Clause itself." *City of Philadelphia v. New Jersey*, 437 U.S. 617, 623 (1978).

Applying traditional pre-emption analysis to this case, California's tax is not pre-empted. There is no specific federal statute with which the tax conflicts and there is no evidence of Congressional intent to pre-empt the field, as indeed there could not be.

The pre-emption test developed in *Japan Line*, to be applied when foreign commerce is at issue, requires that state taxation be pre-empted if it interferes with the "achievement of federal uniformity," 441 U.S. at 450, in what is "pre-eminently a matter of national concern."[16] *Id.* at 448. The broad test enunciated by the *Japan Line* Court would pre-empt a state tax on the basis of a general national policy. *Id.* at 453. The *Japan Line* Court found a national policy to remove impediments on the use of containers in international traffic, and that the county's tax interfered with this policy. *Id.* It found this policy reflected in the Customs Convention on Containers and thus could have found pre-emption of the tax under traditional pre-emption doctrine. Instead it invalidated the tax on broad grounds, stating that "it [the tax] prevent[ed] the Federal Government from 'speaking with one voice' in international trade." *Id.* at 453. By finding a general national policy sufficient to pre-empt the county's tax *Japan Line* departs from other decisions of the Court in which the "national policy" pre-emption standard for finding a conflict between federal and state law was rejected.

The "national policy" pre-emption standard established in *Japan Line* is overly broad. The pre-emption determination must be "guided by respect for the separate spheres of governmental authority preserved in our federalist system." *Alessi v. Raybestos – Manhattan, Inc.*, 451 U.S. 504, 522 (1981). The *Japan Line* standard disregards the resulting canon that federal supremacy is not lightly presumed, *Alessi*, 451 U.S. at 522, by allowing federal pre-emption to be inferred in the absence of "persuasive reasons" of the sort previously required by the Court to invalidate state laws. Because of the importance of

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16 While cases cited by the Court support the idea that uniform treatment of foreign nations is necessary, the *Michelin* Court found that a fairly apportioned non-discriminatory tax would not impair such treatment. 423 U.S. at 286. *See* n. 15, *supra*.

maintaining the state's power to act in its sphere of authority, the national policy standard has been rejected by the Court in traditional pre-emption analysis, regardless of conflict between state law and a general national policy. *Commonwealth Edison*, 453 U.S. at 633-34; *Exxon Corp. v. Governor of Maryland*, 437 U.S. 117, 133 (1978); *New Motor Vehicle Board of California v. Orrin W. Fox Co.*, 439 U.S. 96, 111 (1978). Even in *Commonwealth Edison*, decided after *Japan Line*, the Court stated that it must "look beyond general expressions of 'national policy' to specific federal statutes with which the state law is claimed to conflict." *Id.* at 634 (footnote omitted). In that case the Court agreed that a national policy existed to encourage the use of coal and other alternative fuels instead of petroleum products and natural gas. However, the Court refused to find that this general policy was evidence of a Congressional intent to pre-empt any state regulation which might have an adverse impact on the use of coal. *Id.* Similarly, in *Exxon Corp. v. Governor of Maryland* the Court refused to invalidate a state law which regulated the retail distribution of gasoline even though the law was in conflict with the "basic national policy favoring free competion" which was embodied in the Sherman Act. 437 U.S. at 133. Under the rulings of *Commonwealth Edison* and *Exxon Corp. v. Governor of Maryland*, the existence of a national policy favoring arms-length reporting is not sufficient to pre-empt California's tax, absent a specific federal statutory mandate.

However, even under the broad test announced in *Japan Line* California's tax would not be pre-empted because Container has not shown the existence of even a general national policy with respect to state taxation of multinational corporations. Container argues that California's imposition of a tax determined by apportionment of its multinational income interferes with a federal policy favoring the use of arms-length reporting. This federal policy, Container argues, may be drawn from regulations

promulgated under the Internal Revenue Code and various tax treaties which embody federal schemes for taxing income of multinational corporations. (Brief of Appellant at 29-31) Container cites no specific Congressional action which requires the states to employ arms-length reporting[17] but argues that Congressional intent to pre-empt California's apportioned tax may be inferred from the federal policy. Case law dictates that this inference not be made.

In addition to stating its general reluctance to infer pre-emption, *Exxon Corp. v. Governor of Maryland,* 437 U.S. at 132, the Court has specifically stated that absent an "explicit directive from Congress, [the Court] cannot infer that treatment of foreign income at the federal level mandates identical treatment by the States," *Mobil,* 445 U.S. at 448, because of the "well-established norm" of "[c]oncurrent federal and state taxation." *Id.* The federal regulations and treaties providing for federal taxation of multinational corporations cited by Container are not germane to the issue of state income taxation. *Cf. Mobil,* 445 U.S. at 448. Congress has not issued a directive on the states' power to tax multijurisdictional corporations. This "is attested by the fact that Congress has long debated, but has not enacted, legislation designed to regulate state taxation of income." *Id.* The constitutional taxing system, principles of federalism,[18] the states' sovereign right to

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17 Congress has not taken such a position. *See Mobil,* 445 U.S. at 448.

18 *See* Walter Hellerstein, *State Income Taxation of Multijurisdictional Corporations: Reflections on Mobil, Exxon and H.R. 5076,* 79 MICH.L. REV. 113, 170-71 (1980).

tax[19] and case law preclude a finding that the mere existence of a federal policy for federal taxation of multinational corporations pre-empts state taxing schemes.

Container cites *Moorman*, 437 U.S. at 280, in support of its federal uniformity argument, stating that "the freedom of the States to formulate independent policy in [the] area [of commerce] may have to yield to an overriding national interest in uniformity." (Brief of Appellant at 38) While this quote from *Moorman* is accurate, it is incomplete. The portion omitted by Container makes it clear that this freedom may only yield when Congress enacts "legislation requiring all States to adhere to uniform rules for the division of income." 437 U.S. at 280. *Moorman* clearly holds that "[i]t is to that body [Congress], and not this Court, that the Constitution has committed such policy decisions."[20] *Id.; Accord Common-*

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19 The power to tax is a fundamental attribute of sovereignty, *Gibbons v. Ogden*, 22 U.S. (9 Wheat.) 1 (1824), is "retained by the states. . . [and] is not abridged by the grant of a similar power to the government of the Union . . . [and] is to be concurrently exercised by the two governments. . ." *McCullock v. Maryland*, 17 U.S. (4 Wheat.) 316,425 (1819); *accord Ward v. Maryland*, 79 U.S. (12 Wall.) 418 (1870); *Lane County v. Oregon*, 74 U.S. (7 Wall.) 71 (1869).

20 The entire quote from *Moorman* reads:

> While the freedom of the States to formulate independent policy in this area may have to yield to an overriding national interest in uniformity, the content of any uniform rules to which they must subscribe should be determined only after due consideration is given to the interests of all affected States. It is clear that the legislative power granted to Congress by the Commerce Clause of the Constitution would amply justify the enactment of legislation requiring all States to adhere to uniform rules for the division of income. It is to that body, and not this Court, that the Constitution has committed such policy decisions.

437 U.S. at 280.

wealth Edison, 453 U.S. at 628. Congress has not acted. *Mobil*, 445 U.S. at 448. Therefore, California's tax must stand.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on the 13th day of October, 1982, I, Lisa Gillard Gmuca, a member of the bar of the Supreme Court, caused to be mailed, postage prepaid, three copies of the foregoing Brief of the State of New Mexico as Amicus Curiae in Support of the Franchise Tax Board to Franklin C. Latcham, Counsel for Appellant, One Market Plaza, Spear Street Tower, San Francisco, California 94105 and to George Deukmejiian, Attorney General, and Neal J. Gobar, Deputy Attorney General, Counsel for Appellee, at 110 West A Street, Suite 700, San Diego, California 92101. I further certify that all parties required to be served have been served.

LISA GILLARD GMUCA
Assistant Attorney General